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Supreme Court, U.S.
FILED
DEC 11 1992
OFFICE OF THE CLERK

No. 92-794

In the Supreme Court of the United States

October Term, 1992

COMMONWEALTH OF MASSACHUSETTS, et al,
Petitioners,

v.

GREENWOOD TRUST COMPANY,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

PETITIONERS' REPLY TO THE BRIEF IN OPPOSITION OF RESPONDENT

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The Commonwealth of Massachusetts and the Attorney General of Massachusetts submit this reply to the Brief in Opposition of Respondent Greenwood Trust Company.

1. The Questions Presented are of National Importance

Respondent Greenwood's Brief in Opposition minimizes the legal and practical significance of the decision below. However, the lower court's decision effectively preempts limitations on credit card late charges in all states and seriously impairs the enforcement of state consumer credit laws. See Brief of Amici Curiae of the States of Alaska et al ("Brief of States") at 3 et seq..

Respondent downplays the legal scope of the decision below by suggesting that the decision "simply held that a late charge is 'interest' within the preemptive scope of Section 521." Br. in Opp. 13. The First Circuit's decision was not "simple."

The First Circuit endorses a rule of decision that, in effect, all home-state laws "related to" the determination of the interest rate are exportable. (App. A-25, 26). Since any law with financial significance for the lender might be considered "related to" the determination of the interest rate, there can be no question that this rule of decision limits the force of a wide variety of state consumer credit laws.

The credit card industry has shown no reluctance to challenge state authority and the decision below will weaken considerably that authority.[1/]

1/ See, e.g., Citibank (South Dakota), N.A. v. Thomas J. Miller as Attorney General of the State of Iowa, C.A. 88-258-E (S.D. Iowa 1988)(South Dakota law); United Missouri Bank, U.S.A. v. Thomas J. Miller as Attorney General of the State of Iowa, C.A. 88-1343-E (S.D.

(footnote continued)

The Respondent's brief also suggests that the Commonwealth overstates the dollar amount at stake. (Br. in Opp. at 12). The only estimate the Respondent's brief offers appears at footnote 19, where the Respondent places an upper bound on late charges of $1.7 billion, well above the estimate of $858 million which we cite.[2/]

(footnote continued)

Iowa, C.A. 88-1343-E (S.D. Iowa 1988) (Delaware law); and United Missouri Bank of Kansas City v. Thomas J. Miller as Attorney General of the State of Iowa, C.A. 88-1344-E (S.D. Iowa 1988) (Missouri law), in which foreign state credit card lenders challenged Iowa laws restricting late charges, returned check fees, attorney's fees, and changes in cardholder term requirements. These cases were settled without a judicial decision on the merits.

2/ Pet. 16, 17. Greenwood cites to The Nilson Report (November 1991) for the statement that revenues from late charges were "less than 5% of revenues" in 1991. (Br. in Opp. 13, fn. 19) Since that same Report (at 5) also

(footnote continued)

At the same time that it downplays the importance of the decision, Respondent conjures grave consequences of reversal. Greenwood speculates without support that "unfriendly legislation," aimed at federally insured banks, will grow from the hostile soil of state legislatures if this Court rightly narrows the meaning of

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(footnote continued)

indicated that credit cards generated approximately $34.24 billion in revenues in 1991, Respondent's statement means that late charge revenues were not above $1.7 billion in 1991.

Respondent also incorrectly implies that the additional interest charges allowed under Marquette, Marquette National Bank v. First of Omaha Service Corp., 439 U.S. 299 (1978), dwarf the late charges at stake in the current case. Br. in Opp. 19. In fact, the charges Marquette made legal are only a portion of all interest charges (the portion in excess of the interest rate ceiling of the state of the cardholder).

"interest" to conform with Congressional intent. (Br. in Opp. 6, text and fn. 5).[3/]

2. The First Circuit's Preemption Analysis is Inconsistent with Decisions of this Court

The decision below, despite Greenwood's claim to the contrary, cannot be reconciled with the preemption principles set out in Cipollone v. Liggett Group, Inc., 112 S.Ct 2608 (1992). That the First Circuit's opinion "is replete with citations to Cippollone" (Br. in Opp. 11) reveals only an awareness of, not an adherence to, Cipollone.

Respondent asserts that the First Circuit found that Congress's "intent to

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3/ The Massachusetts law, Mass. Gen. Laws Ann., ch. 140, §114B (West 1991), like other modern consumer credit legislation, regulates evenhandedly. The Commonwealth does not seek an upper hand vis-a-vis federally chartered or out-of-state lenders; it simply seeks to enforce its consumer protection laws consistently.

displace state law is clear." (Br. in Opp. 11). However, the First Circuit went on to find explicitly the absence of clear intent by Congress to preempt late charge laws. It stated that "DIDA's text and legislative history are, at bottom, inconclusive" as to the meaning of "interest" and "interest rate." (App. A-41). Its preemptive holding was founded on a line of usury (not preemption) cases. These cases were shaped by a judicial desire to support law enforcement of usury laws; they do not stand for the proposition that late charges are "interest," only that some loan charges should be computed-in along with percentage interest for the purpose of applying usury laws (to prevent circumvention of those laws). By contrast, in this case, "interest" must be narrowly construed so

as to comply with the clear statement requirement for preemption.

The intent to preempt must be clearly communicated in determining the scope of express preemption. See "Brief of States" 8-11. Cipollone stands for the proposition that even in an express preemption case, a court must find against preemption in cases where the borders of the scope of preemption are not clear. In Cipollone, this Court stated that the presumption against preemption "reinforces the appropriateness of a narrow reading" of express preemption clauses. Cippollone, 112 S.Ct. at 2618.[4/]

4/ In a separate opinion joined by Justices Kennedy and Souter, Justice Blackmun underlined this narrow reading: "We do not, absent unambiguous evidence, infer a scope of pre-emption beyond that which clearly is mandated by Congress' language." Cipollone, 112 S. Ct. at 2626.

The court below explicitly found no intent to preempt late charge regulation in Congress' language. Its finding that state law charge laws may be preempted by ambiguous federal law is incompatible with this Court's preemption decisions. See Pet. 30-35.

3. The First Circuit's Decision is Not Compelled by Marquette

Greenwood insists that the decision below follows inexorably from Marquette, supra. (Br. in Opp. 12-13). Although Marquette speaks to the definition of the term "located" in Section 85 of the National Bank Act (12 U.S.C. 85), it is completely silent on the meaning of the term "interest."

More generally, Respondent portrays Marquette and DIDA as creating a "level playing field" for the various players in interstate banking by allowing banks

competing in multiple states to avoid the complexity of differing regulatory regimes. (Br. in Opp. 4-6, 11). This mischaracterization became an important policy rationale for the broad preemptive holding of its decision. (App. A-51). In fact, as developed in our Petition, banks have always worked within a regime of multiple regulation. (Pet. 35-42).

Greenwood specifically asserts that "forcing credit card issuers to vary their late charges by state to comply with disparate state laws would engender the very confusion Marquette sought to avoid" (Br. in Opp. 11). In fact, Marquette avoided a different "confusion". Marquette held that a national bank is "located" only in its home state for the purpose of applying

Section 85. Marquette 439 U.S. at 313.

> "If the location of the bank were to depend on the whereabouts of each credit card transaction, the meaning of the term 'located' would be so stretched as to throw into confusion the complex system of interstate banking". Marquette, 439 U.S. at 312 (emphasis added).

Asking banks to comply with the late charge laws of the cardholder's home state is far less confusing than requiring that every card transaction be governed by the law of the state in which it occurs.

Respondent also suggests that the Commonwealth is making a policy defense of state usury laws weakened by Marquette. (Br. in Opp. 15). To the contrary, we explicitly accept the holding of Marquette as it applies to state interest rate laws (but reject Respondent's attempt to extend it to late charge laws). (Pet. 41).

Marquette did not impute to Congress an intent to create a uniform scheme of regulation under the guise of section 85 of the National Bank Act. Nor did it sanction the preemption of state laws other than percentage interest rate restrictions. To the extent that Greenwood seeks to further this policy concept, it should address itself to Congress. See Marquette, 439 U.S. at 319. It is Greenwood, not the Commonwealth, that is seeking a judicial revision of Congressional policy.

4. DIDA Does Not Preempt Late Charge Laws

Respondent states that "Courts have long recognized the need to construe 'interest' . . . to effectuate the 'most favored lender' doctrine." (Br. in Opp. 5). The Commonwealth agrees.

Similarly, Respondent characterizes as a concession and emphasizes our acknowledgement that "in usury cases, courts must include as interest some fees and charges associated with loans." By reviewing case law on these points at length, Respondent is, in a self-serving way, defining incorrectly the issue at hand. This is not a most-favored-lender case, nor is it a usury case. Massachusetts late charge law applies to all lenders, foreign and domestic, and Massachusetts is not attempting to apply usury law to restrict Respondent's overall economic returns from its loans. (Pet. 13-15).

Greenwood responds to these fundamental distinctions by asserting that "If Greenwood's late charge 'must' be treated as 'interest' under Section

521 for usury purposes, it must likewise be considered 'interest' under Section 521 for preemption purposes." (Br. in Opp. 9). (It is important to note that the Commonwealth does not concede that late charges as opposed to some other charges, must be treated as interest under Section 521 for usury purposes. Pet. 42-49.) The clumsy simplicity of respondent's assertion misconstrues the Commonwealth's argument and ignores fundamentals of legal reasoning. In the words of Justice Holmes:

> "A word is not a crystal, transparent and unchanged, it is the skin of a living thought, and may vary greatly in color and content according to the circumstances and the times in which it is used."

Towne v. Eisner, 245 U.S. 418, 425 (1918). "Interest" is undoubtedly one of the fundamental concepts of finance,

and like all fundamental concepts does apply differently in different contexts. Many fundamental legal concepts have been found to have this "protean" quality.[5/] There is nothing incongruous about construing the term "interest" broadly in doing usury computations and narrowly in deciding preemption issues. In fact, Cipollone, supra, compels this.

Respondent asserts that the legislative history of the recodification of Section 522 of DIDA in

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5/ See, e.g., references to protean qualities of "implied preemption" (decision of First Circuit at App. A-13, citing French v. Pan Am Express, 869 F.2d 1, 2 (1st Cir. 1989); "jurisdiction" (Sweeney v. Westvaco Co., 926 F.2d 29, 40 (1st Cir. 1991); "fraud" (United Electrical Radio and Machine Workers v. 163 Pleasant Street Corp., 960 F.2d 1080, 1093) (1st Cir. 1992); and "good cause" (U.S. v. De Jongh, 937 F.2d 1, 5 (1st Cir. 1991).

1989 may be read as confirming the position that late charge regulations are preempted by Section 521. (Br. in Opp. 14, 15). This asertion is wrong for three reasons: (1) The passage cited does not broaden the meaning of the term interest to include "loan related charges." The Respondent clips the passage, which in its entirety, refers to preemption only where state law prescribes a rate below a specified numerical percentage rate defined with reference to the rates on 90 day commercial paper. See Appendix. (2) In the words of the Respondent at Br. in Opp. 15, "DIDA was a hodgepodge of diverse and unrelated provisions . . . [and] "there is no evidence that Congress intended 'interest' to have a single meaning throughout all of Title V

of DIDA." (3) The case law cited by the respondent as to the general relevance of the authority offered is inapposite.[6/]

Greenwood also asserts that the First Circuit's opinion is merely one decision "in a long and unbroken line of decisions that uniformly have held a wide variety of fees and charges to

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6/ In Red Lion Broadcasting Co. v. FCC, 395 U.S. 367, 381, later modification of the statutory language itself was used to understand the original intent of the statute. In the Respondent's brief, the authority offered is not statutory language but legislative history (and of a different statute).

Similarly weak is Respondent's argument that Congress was aware of, but chose to condone, the violation of state late charge laws by interstate credit card companies. In Board of Governors v. First Lincolnwood Corp., 439 U.S. 234, 248 (1978), unlike the present case, where Congressional inaction was taken as an endorsement of an industry practice, Congress had held repeated hearings on the subject at hand.

constitute 'interest' ..." (Br. in Opp. 3). That representation is misleading because it suggests that all fees and loan related charges may be fairly characterized as "interest."

The critical factor in distinguishing between "interest" and "late charges" is not the label of the charge, but the substance of the transaction. Greenwood ignores the clear distinction between upfront charges and default charges. Upfront charges, imposed at the inception of the loan as compensation and a condition for the loan itself, fall within longstanding definitions of "interest." Default charges, imposed only upon default, are avoidable, or are contingent on the performance of the borrower; they are not compensation for

the loan. Greenwood's late charges are contractual default charges; they are not "interest." Greenwood has not cited any pre-1992 case holding under Sec. 521 of DIDA or Sec. 85 of the National Bank Act that a single sum late fee or other default related fee should be included in the calculation of "interest."[7/]

7/ In fact, in the only pre-1992 case cited by Greenwood where the court considered a lending charge that was not charged upfront (prepayment charge), the parties assumed that the charge was not "interest" because the payment of the charge was within the control of the borrower. See Northway Lanes v. Hackley Union Nat'l Bank & Trust Co., 464 F.2d 855, 864 (6th Cir. 1972) (Br. in Opp. 6-7).

CONCLUSION

It is therefore respectfully submitted that the petition for a writ of certiorari should be granted.

Respectfully submitted,

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Appendix

H.R. Rep. No. 54 at 343
(101st Cong., Sess., pt 1) (1989)

This section provides that a savings association may take, receive, reserve, or charge on any loan, note, bill of exchange, or other evidence of debt, interest at the greater of (1) a rate not more than one per centum in excess of the discount rate on ninety-day commercial paper in the specified Federal Reserve Bank where the institution is located, or (2) the rate allowed by the laws of the State where such institution is located. If such rate exceeds the rate that would be permitted in the absence of this section, such rate may be employed notwithstanding any State constitution or statute concerning loan related charges, which is thus preempted. The effect of this section is to preserve the current preemption of state usury laws.